

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This management discussion and analysis ("MD&A") was performed by management using information available as of February 19, 2010 and should be read in conjunction with our unaudited interim consolidated financial statements and notes thereto for the three and nine months ended December 31, 2009, as well as audited consolidated financial statements and notes thereto and the MD&A for the year ended March 31, 2009. All financial information has been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"), and all amounts are expressed in Canadian dollars unless otherwise indicated. Additional information relating to Pacgen Biopharmaceuticals Corporation (the "Company") can be obtained from SEDAR at www.sedar.com.

The forward-looking statements in this discussion regarding our expectations of our future performance, liquidity and capital resources and other non-historical statements include numerous risks and uncertainties, as described in note 5 in our unaudited interim consolidated financial statements, in the "Risks and Uncertainties" section of our annual MD&A dated July 9, 2009, and in the "Risk Factors" section of our Annual Information Form dated July 31, 2008, which are available on SEDAR at www.sedar.com. The words "anticipates", "believes", "estimates", "expects", "intends", "may", "could", "plans", "projects", "will", "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. Such statements involve known and unknown risks, uncertainties and other factors that may cause actual results, level of activity, performance or achievements to be materially different from those implied by such statements. Such factors include, among others, our stage of development, lack of product revenues, additional capital requirements, risk associated with completion of clinical trials and obtaining regulatory approval, dependence on collaborative partners, our ability to protect our intellectual property, and our ability to stay competitive in a rapid changing industry environment. We undertake no obligation to revise or update forward looking statements in this discussion whether as a result of new information, future events or otherwise. Accordingly, readers should not place undue reliance on forward looking statements in this discussion.

OVERVIEW

We are a life science technology transfer company focused on the commercial development of novel therapeutic drug candidates up to Phase II, proof of concept efficacy in human. We identify innovative therapeutic drug candidates globally, and develop these drug candidates in accordance to the United States Food and Drug Administration (the "FDA") regulatory standards to feed the product development pipelines of the pharmaceuticals industry. We currently have two product pipelines in our technology portfolio: PAC-113, an anti-fungal for the treatment of oral Candidiasis, and PAC-G31P, a novel peptide therapeutic designed to treat inflammatory diseases characterized by non-beneficial neutrophil.

PAC-113 is a 12 amino-acid antimicrobial peptide derived from a naturally occurring histatin protein found in saliva. This peptide alters the permeability of fungal cell membranes causing cell death. We are developing PAC-113 in a mouthrinse formulation for the topical treatment of oral Candidiasis. Oral Candidiasis, or thrush, is usually seen as a secondary consequence arising from one of a number of primary or underlying medical conditions including HIV/AIDS, cancer, diabetes, asthma and xerostomia (abnormal dryness of the mouth). We obtained our rights to PAC-113 through a sublicense agreement with Demegen, Inc. (the "Demegen Sublicense") in February 2005. The Demegen Sublicense provides us with exclusive worldwide rights to develop and commercialize PAC-113 for human oral disease conditions. Since obtaining these rights, we have completed formulation optimization work, a Phase I/II proof of concept clinical study, as well as a Phase IIb dose-ranging study. The data from our clinical studies demonstrates that PAC-113 is effective in the treatment of oral Candidiasis. The data also suggests that PAC-113 compares favourably to the efficacy demonstrated by Nystatin, a current standard of care. We are currently working with a collaborative partner to develop PAC-113 for the treatment of oral Candidiasis for commercialization in China. We are also seeking for joint-venture / co-development partners for regions outside of China.

PAC-G31P is a small recombinant protein that is a synthetic analogue of the human cytokine called Interleukin-8 which is the key chemokine involved in neutrophil recruitment. We are developing PAC-G31P to treat

inflammatory diseases. Non-beneficial neutrophil recruitment is a key characteristic of a number of acute and chronic inflammatory conditions, including acute respiratory distress syndrome, severe asthma, chronic obstructive pulmonary disease, pneumonia, Crohn's Disease, rheumatoid arthritis and ischemia/reperfusion injury. We obtained exclusive worldwide rights to PAC-G31P technology for the prevention and treatment of severe inflammatory diseases characterized by neutrophil over-recruitment in April 2006, through the acquisition of IL Therapeutics Inc. ("ILT"). Since taking over the PAC-G31P program, we conducted a number of preclinical and mechanistic studies, and initiated formulation development work. PAC-G31P is currently in preclinical development. We are currently seeking for a joint-venture or co-development partner to conduct preclinical and toxicology studies, as well as manufacturing work necessary to enable a filing of Investigational New Drug application ("IND").

We currently hold the rights to 26 patents and 31 patent applications in the United States and other jurisdictions relating to products in our development pipeline. We also hold 2 granted patents and 7 patent applications and intellectual properties to two other research compounds that we no longer develop.

CORPORATE DEVELOPMENT EVENT

During the quarter ended December 31, 2009 ("Q3 2010"), the Company actively pursued a number of business development leads in the emerging markets in Asia. These business development efforts had led to a collaborative research and development deal with Shanghai based New Summit Biopharma Co. ("New Summit Bio"). Subsequent to Q3 2010, both parties entered into collaboration research and development agreements in January 2010. Under the terms of the collaborative research and development agreements, New Summit Bio will collaborate with the Company to raise funding and develop PAC-113 for the Chinese market.

STATUS OF RESEARCH AND DEVELOPMENT PROJECT

PAC-113

Based on our Phase IIb clinical trial results obtained in June 2008, PAC-113 is effective in the treatment of oral Candidiasis and compares favorably to efficacy demonstrated by Nystatin. Nystatin is a current standard of care for topical treatment of oral Candidiasis. The next development milestone for PAC-113 is to meet with regulatory authority to discuss pivotal clinical trial design and development plan.

During Q3 2010, other than the continuation of certain stability studies of PAC-113, we did not initiate any new research and development studies. Following a comprehensive review in the preceding fiscal year (the "Fiscal 2009"), we elected to defer further development of PAC-113 until a collaborative partner is secured and new funding is raised. Subsequent to Q3 2010, we entered into collaboration research and development agreements with New Summit Bio to develop PAC-113 for the treatment of oral Candidiasis. Under the terms of the agreements, New Summit Bio will collaborate with us to raise funding and develop PAC-113 for the Chinese market. We plan to continue our efforts to pursue additional partnership for PAC-113 with collaborative or joint-venture partner for market outside of China. Despite these efforts, there can be no assurance that development funding will be secured by our Chinese collaborative partner, or that additional partnership or joint-venture will be secured for market outside of China.

PAC-G31P

Based on data generated from our previous preclinical and mechanistic studies, we believe PAC-G31P has the potential to treat inflammatory diseases characterized by neutrophil over-recruitment. The next development milestones for PAC-G31P are to determine the optimal first clinical indication and to conduct IND enable studies, including preclinical and toxicology studies, as well as manufacturing work.

During Q3 2010, we did not initiate any new research and development studies for PAC-G31P due to financial constraints. Our operational efforts were focused primarily on seeking for a joint-venture or co-development partner. We plan to continue our efforts to secure partnering leads for PAC-G31P. Despite these efforts, there can be no assurance that a collaborative partnership or joint-venture will be secured on a timely basis or with favourable terms, if at all.

SELECTED CONSOLIDATED FINANCIAL INFORMATION

The following table sets forth consolidated financial data for the fiscal years ended March 31, 2009, 2008 and 2007:

	For the year ended March 31,		
	2009	2008	2007
Net loss for the period	\$(2,282,640)	\$(5,974,712)	\$(4,353,837)
Per share loss, basic and fully diluted	\$(0.06)	\$(0.19)	\$(0.20)
Total assets	\$1,676,523	\$3,024,237	\$7,834,666
Long-term liabilities	\$216,459	—	—

RESULTS OF OPERATIONS

Overall Performance

For Q3 2010, we recorded a net loss of \$468,181 (\$0.01 per common share), compared to a net loss of \$21,698 (\$0.00 per common share) for the three months ended December 31, 2008 (“Q3 2009”). On a year-to-date basis, we recorded a net loss of \$1,110,484 (\$0.03 per common share), compared to a net loss of \$1,971,653 (\$0.06 per common share) for the same period in the preceding fiscal year. The higher net loss in Q3 2010, as compared to Q3 2009, was primarily due to a recovery of \$746,516 (approximately US\$603,000) of research and development expenditures in Q3 2009, which was offset by reduced operating expenditures in the current fiscal period. The decreased net loss on a year-to-date basis was mainly due to our reduced operating expenditures in the current fiscal period.

Since we commenced operations in April 2004, we have accumulated a deficit of \$15,940,805 as at December 31, 2009. We have not generated any revenue from product sales to date and expect to incur continuing operating losses in the foreseeable future. We are considered to be in the development stage. Our ability to continue as a going concern is dependent upon our ability to obtain additional financing. We have funded our operations primarily by share issuances in the past. As at December 31, 2009, we had cash and cash equivalents of \$30,107 and a working capital deficiency of \$1,636,754. Given our working capital deficiency as at December 31, 2009, it is critical that we raise new funding in the near future to continue our operations.

The global economic crisis in 2009 has led to a substantial reduction in capital in the credit markets, especially for companies in the development stage. Despite some signs of economic improvement in the general financial market, smaller life science technology companies, which are generally viewed as higher risk investments, continue to encounter difficulty in raising new capital. Given this challenging credit market environment, we continue to conserve cash and pursue all possible alternatives to secure additional capital to finance our operations. We have encountered resistance from new and existing shareholders to raise additional capital due to our current outstanding liabilities. We have initiated discussions with our creditors to reduce or restructure our liabilities in order to enhance our ability to raise funds. While management believes these efforts may lead to a near term financing, there can be no assurance that such financing will be materialized or be completed on a timely basis and on favorable terms. If we are unable to obtain additional financing, we may be required to cease our operations.

Our financial statements have been prepared in accordance with Canadian GAAP applicable to a going concern, which assumes that we will be able to meet our obligations and continue our operations for the next twelve months. Realization values may be substantially different from the carrying values as shown and these financial statements which do not give effect to adjustments that would be necessary to the carrying values and classifications of assets and liabilities should we be unable to continue as a going concern. If the going concern assumption was not used, adjustments required to report our assets and liabilities, as well as to report on our net loss, on a liquidation basis could be material.

Revenues

We have not generated any revenue from sales of commercial products since our incorporation and we do not expect to generate any revenues in the foreseeable future.

Research and Development Expenditures

Research and development expenses were \$19,675 for Q3 2010, as compared to \$208,858 for Q3 2009. On a year-to-date basis, research and development expenses for the nine months ended December 31, 2009 (“YTD 2010”) were \$71,297, compared to \$1,245,309 for the nine months ended December 31, 2008 (“YTD 2009”). The research and development expenses in both Q3 2009 and YTD 2009 were reduced by a recovery of out of scope charges from a vendor of \$746,516 (approximately US\$603,000). The decreases of research and development expenses in both periods were primarily due to our reduced research and development activities. We have deferred further development of our programs until new development funding is secured either through our existing or new collaborative partnership.

The following provides a summary of the research and development expenditures by programs for the comparative three and nine months ended December 31, 2009 and since inception:

Projects	For the three months ended		For the nine months ended		Cumulative from
	2009	2008	2009	2008	Inception to December 31, 2009
PAC-113 (2005 – 2009)					
Expense	\$17,731	\$181,502	\$61,372	\$1,109,120	\$5,530,517
Recovery	—	(746,516)	—	(746,516)	(865,287)
	17,731	(565,014)	61,372	362,604	4,665,230
PAC-G31P (2007 – 2009)	1,944	10,308	12,494	111,927	2,112,098
Other Projects	—	17,048	(2,569)	24,262	210,996
	\$19,675	\$(537,658)	\$71,297	\$498,793	\$6,988,324

PAC-113

PAC-113 development cost, before expense recovery, declined by \$163,771 in Q3 2010 as compared to those in Q3 2009. The decrease was mainly due to our decision to defer further development of PAC-113 until new development funding is secured through collaborative partnership. The development cost in Q3 2010 covered primarily the maintenance of license and patents, while those in Q3 2009 covered primarily the costs associated with our Phase IIb study and the maintenance of license and patents. We recovered \$746,516 (approximately US\$603,000) of the Phase IIb development cost after receiving a credit note from a vendor in Q3 2009.

The development cost, before expense recovery, decreased substantially by \$1,047,748 in YTD 2010 as compared to those in YTD 2009. The significant reduction in development cost was due to the minimal development activities following the completion of Phase IIb clinical trial in June 2008. The development cost in YTD 2010 covered mainly the maintenance of license and patents, while those in YTD 2009 covered the costs associated with Phase IIb clinical trial, as well as the maintenance of license and patents.

For the remaining quarter in the current fiscal year ending March 31, 2010 (“Fiscal 2010”), we expect to incur minimal research and development expenditures for PAC-113. The expected research and development cost comprises the cost associated with license and patent maintenance as well as stability studies.

PAC-G31P

PAC-G31P research cost decreased by \$8,364 in Q3 2010 as compared to those in Q3 2009. Research expenditure in both Q3 2010 and Q3 2009 covered primarily the maintenance of patents. The research cost decreased by \$99,433 in YTD 2010 as compared to those in YTD 2009. Research expenditure in YTD 2010 covered primarily the maintenance of patents, while those in YTD 2009 composed mainly of the maintenance of patents and the internal overhead associated with our research personnel. The decreases for both periods were due to the reduced research activities associated with this project.

For the remainder of Fiscal 2010, we expect to incur minimal research and development expenditures for PAC-G31P. The expected research and development cost comprises the cost associated with license and patent maintenance.

General and Administration Expenditures

General and administration expenses were \$103,445 for Q3 2010, compared to \$277,673 for Q3 2009. On a year-to-date basis, general and administration expenses were \$417,136, compared to \$881,375 for the same period in the preceding fiscal year. General and administration expenses were significantly lower in both Q3 2010 and YTD 2010 as compared to the same periods in the preceding fiscal year. The decrease in general and administration expenses was primarily due to the implementation of our cost control programs.

The following provides a summary of the general and administration expenditures for the comparative three and nine months ended December 31, 2009 and since inception:

General and Administration Expenditures	For the three months ended		For the nine months ended		Cumulative from
	December 31,		December 31,		Inception to
	2009	2008	2009	2008	December 31, 2009
Consulting and management fees	\$47,352	\$15,410	\$144,995	\$212,777	\$984,110
Market research and business development	—	—	58,490	—	179,728
Professional fees	14,526	146,906	36,467	221,396	1,020,631
Salaries and benefits	—	68,577	900	279,901	2,441,614
Travel and accommodation	1,230	6,931	39,860	36,756	377,267
Other general overhead	40,337	39,849	136,424	130,545	1,440,586
	\$103,445	\$277,673	\$417,136	\$881,375	\$6,443,936

Consulting and management fees recorded in Q3 2010 were related to management fees of Xphase principals. Of the purchase price of our acquisition of Xphase Pharmaceuticals Inc. ("Xphase Acquisition"), completed in the previous quarter, \$189,407 was allocated to management services acquired. This allocation of purchase price was amortized over a one-year service period starting April 1, 2009. Consulting and management fees in YTD 2010 were primarily the management fees of Xphase principals, while those in YTD 2009 were primarily related to business development activities.

Market research and business development expenditures increased in YTD 2010, as compared to the same period in the preceding year, due to our in-licensing activities in an effort to enhance our financing ability. Professional fees declined in both Q3 2010 and YTD 2010, as compared to those in the same periods in the preceding fiscal year, mainly due to our cost cutting measure to internalize work in-house whenever possible. Salaries and benefits also declined as a result of eliminating management salaries. All full-time positions have been replaced with management consultant positions which are compensated by stock based compensation. Travel and accommodation expenditures as well as other general overhead in both Q3 2010 and YTD 2010 were comparable to those in the same periods in the preceding fiscal year.

For the remainder of Fiscal 2010, we expect our general and administration expenditures to be relatively the same as those incurred during the nine months ended December 31, 2009. In accordance to the terms of the Xphase Acquisition, Xphase principals will provide management and business development services for equity based compensation.

Stock Based Compensation

Stock based compensations, a non-cash item included in operating expenses, attributable to research and development activities or general and administration activities are as follows:

Stock Based Compensation	For the three months ended		For the nine months ended		Cumulative from
	December 31,		December 31,		Inception to
	2009	2008	2009	2008	December 31,
Research and development	\$ -	\$ 8,820	\$ 24,814	\$ 56,319	\$ 453,677
General and administration	109	42,590	101,922	145,247	835,749
	\$109	\$51,410	\$126,736	\$201,566	\$1,214,597

Other than the residual amount of \$109 recorded in Q3 2010, stock based compensations for all stock option grants including those to Xphase principals, have been recognized in prior periods. The decreases in stock based compensation in Q3 2010 and YTD 2010, as compared to the same periods in the preceding year, were mainly due to the reduced number of stock options granted and increased number of stock options forfeited or cancelled. Starting April 2009, our compensation package to internal personnel includes only stock based compensation. In addition to stock option grants, Xphase principals also received our common shares from the Xphase Acquisition for their management services.

For the remainder of Fiscal 2010, we may grant new options to certain consultant and expect our stock based compensation to be minimal.

Amortization and Write-down of Intangible Assets

Amortization was \$63,267 in Q3 2010, compared to \$66,307 in Q3 2009. Year-to-date amortization was \$189,794, compared to \$198,921 for the same period in the preceding fiscal year. Amortization related to technology, licenses and rights in Q3 2010 remained the same at \$59,244, compared to Q3 2009. The remaining amortization was related to property and equipment.

We wrote off \$244,408 of the net book value of our intangible assets in Q3 2010 to reflect the impairment in value of our PAC-G31P license given the uncertainty surrounding the funding of this project. As of December 31, 2009, we have not secured any collaborative partner or new funding to continue our development of PAC-G31P.

Other Income (Loss)

Other loss was \$37,277 in Q3 2010, compared to \$163,966 in Q3 2009. On a year-to-date basis, other loss was \$61,112, compared to \$190,998 for the same period in the preceding fiscal year. The decreases in other loss for both periods were mainly due to higher foreign exchange gains, which were offset by higher financing and interest expenses and reduced interest incomes. The financing and interest expenses of \$65,541 in Q3 2010 and \$202,254 in YTD 2010 were associated with an amount payable to a vendor and the convertible debentures issued in Fiscal 2009. The reduced interest income was primarily due to our lower cash balances. The increases in net foreign exchange gain for both periods were due to the depreciation of the United States dollar, in comparison with the Canadian dollar, on our US denominated retainer payments, accounts payable and accrued liabilities, and other payable.

SUMMARY OF QUARTERLY RESULTS

Set forth below is the selected consolidated financial data for each of the last eight quarters:

	3rd Quarter Ended December 31, 2009 ("Q3 2010")	2nd Quarter Ended September 30, 2009 ("Q2 2010")	1st Quarter Ended June 30, 2009 ("Q1 2010")	4th Quarter Ended March 31, 2009 ("Q4 2009")
Research and development	\$(19,675)	\$(14,916)	\$(36,706)	\$(87,804)
General and administration	(103,445)	(259,210)	(54,481)	(118,457)
Stock based compensation	(109)	(95,933)	(30,695)	40,879
Amortization	(63,267)	(63,341)	(63,186)	(64,895)

Write-down of intangible assets	(244,408)	—	—	—
Other income (loss)	(37,277)	100	(23,935)	(80,710)
Future income tax recovery	—	—	—	—
Net loss for the period	(468,181)	(433,300)	(209,003)	(310,987)
Basic and diluted loss per common share	\$(0.01)	\$(0.01)	\$(0.01)	\$(0.01)

	3rd Quarter Ended December 31, 2008 ("Q3 2009")	2nd Quarter Ended September 30, 2008 ("Q2 2009")	1st Quarter Ended June 30, 2008 ("Q1 2009")	4th Quarter Ended March 31, 2008 ("Q4 2008")
Research and development	\$537,658	\$(155,264)	\$(881,187)	\$(1,071,903)
General and administration	(277,673)	(298,815)	(304,887)	(307,439)
Stock based compensation	(51,410)	(91,346)	(58,810)	(119,597)
Amortization	(66,307)	(66,307)	(66,307)	(63,905)
Write-down of intangible assets	—	—	—	—
Other income (loss)	(163,966)	(30,722)	3,690	(129,095)
Future income tax recovery	—	—	—	27,722
Net loss for the period	(21,698)	(642,454)	(1,307,501)	(1,664,217)
Basic and diluted loss per common share	\$(0.00)	\$(0.02)	\$(0.04)	\$(0.05)

Summary of Quarterly Results

The primary factors affecting the magnitude of our losses in the various quarters were (i) expenditures associated with our PAC-113 Phase IIb clinical trial (ii) recovery of part of our Phase IIb clinical expenditures (iii) the implementation of our cost programs in different stages in the preceding two fiscal years.

Research and development expenditures were in declining trend since Q4 2008 as a result of (i) our decision, in November 2007, to focus our development efforts primarily on the completion of PAC-113 Phase IIb clinical study and to scale down of PAC-G31P research and development activities and (ii) our decision, following the completion of the Phase IIb study in June 2008, to defer further development of all projects until collaborative or joint venture partners are secured. The net recovery of research and development expense of \$537,658 in Q3 2009 was primarily due to a cost recovery of \$746,516 (approximately US\$603,000) associated with PAC-113 Phase IIb and an underlying accretion of interest of \$118,073 in Q4 2009, following our renegotiation with a vendor.

General and administration expenditures were in a declining trend, except in Q2 2010, as a result of our cost control programs implemented in the preceding two fiscal years. The cost control programs involved (i) replacement of all full-time positions with consultant positions (ii) appointment of Chairman of our board of directors to act as interim President and Chief Executive Officer, for the period of November 2008 to August 2009, at no compensation, and (iii) elimination of all director fees effective February 2008. The increase of general and administration expenditures in Q2 2010, as compared to Q1 2010, was primarily due to the increased management fees following the appointment of Xphase principals as our management, and the increased market research and business development cost associated with our partnering activities.

LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash

Since inception to December 31, 2009, our operational activities were financed mainly from equity financings, other than the recent issuance of convertible debentures in Q4 2009 and the cash acquired from ILT in April 2006.

Cash used in operating activities for Q3 2010 was \$18,875, compared to \$199,352 for Q3 2009. Year-to-date cash used in operating activities was \$256,110, compared to \$1,398,470 for the same period in the preceding fiscal year. Cash used in operating activities was composed of net loss, add-backs or adjustments not involving cash and net change in non-cash working capital items. The decrease of cash used in operating activities in each of the current fiscal periods was primarily due to the reduced net loss after adding add-back of non-cash items, and the reduced cash disbursements for changes in non-cash working capital.

Cash used in investing activities for YTD 2010 was primarily related to the transaction costs in relation to the Xphase Acquisition. There was no cash used in investing activities in Q3 2010, Q3 2009 and YTD 2009. There is no cash provided by financing activities for the reporting periods in current or previous fiscal year.

As of December 31, 2009, we had available cash reserves comprised of cash and cash equivalents of \$30,107, compared to \$308,871 at March 31, 2009. We had a working capital deficiency of \$1,636,754 at December 31, 2009, compared to \$1,023,213 at March 31, 2009. We are currently seeking additional capital to finance our operations and obligations. Management is considering all possible financing alternatives, including equity financing, debt arrangement and corporate collaboration, and has initiated discussions with our creditors to reduce or restructure our liabilities in order to enhance our financing ability. There can be no assurance that such financing will be materialized or be completed on a timely basis to allow us to continue as a going concern. If we are unable to obtain new funding, we may be required to cease our operations in the near term.

As of December 31, 2009 and in the normal course of business we have obligations to make future payments, representing contracts and other commitments that are known, committed, cancellable and non-cancellable.

	Contractual Obligations payment due by period				
	Total	2010	2011-2012	2013-2014	Thereafter
Operating Leases	\$82,271	\$32,140	\$50,131	—	—
Clinical Research Agreements ⁽¹⁾	1,978,610	1,978,610	—	—	—
License Agreements ⁽²⁾⁽³⁾	328,438	13,138	105,100	105,100	105,100
Total	\$2,389,319	\$2,023,888	\$155,231	\$105,100	\$105,100

⁽¹⁾ The total commitment of \$1,978,610 reflects \$6,775 of commitments that are non-cancellable and \$1,971,835 of commitments that are cancellable, including those commitments that require forfeiting of prepaid amounts of US\$382,261 (\$401,757) if commitments are cancelled.

⁽²⁾ Pursuant to the Demegen Sublicense, which relates to our PAC-113 licensed technology, we have a commitment to pay minimum annual royalties of US\$50,000 as described in *note 9(a)* of our annual consolidated financial statements for the fiscal year ended March 31, 2009. This commitment is converted into Canadian Dollars at the closing rate on December 31, 2009 of CAD\$1.00 = US\$0.9515. All minimum royalties other than, US\$7,000 for 2008 and US\$50,000 for 2009, were paid as of December 31, 2009. We have obtained acknowledgement from the licensor that the outstanding minimum annual royalties of US\$57,000 would be deferred until a financing is secured. We are in discussion with the licensor to arrange for settlement of the outstanding royalty of US\$57,000. While we believe that our ongoing communication with the licensor has kept us in good terms, there can be no assurance that the licensor would not demand full payment or return of the Demegen Sublicense in the near term. Our research and collaboration with New Summit Bio is contingent upon our ability to maintain the Demegen Sublicense in good terms

- (3) Pursuant to a license agreement between ILT and the University of Saskatchewan (the “US License”), we have a commitment to sponsor \$500,000 for research related to the licensed technology PAC-G31P, to be performed at the University of Saskatchewan within 5 years of the term of the agreement. As of December 31, 2009, we have paid \$334,097 and accrued \$60,000 of contract research fees for research studies conducted by the university. The remaining balance of \$105,903 was due for commitment on October 15, 2009. The Company is in discussion with the university to waive the remaining funding commitment of \$105,903, and to arrange for settlement of the outstanding research contract fees of \$60,000 and patent reimbursements of \$107,175. While we believe that our ongoing communication with the university has kept us in good terms, there can be no assurance that the university would not demand immediate payment for all outstanding amounts or return of the US License in the near term.

OUTSTANDING SHARE CAPITAL

As of February 19, 2010, there were 38,144,693 common shares issued and outstanding, 4,656,933 common share purchase warrants outstanding at a weighted average price of \$0.30 per share, and 2,960,000 incentive stock options outstanding at a weighted average exercise price of \$0.44.

OFF-BALANCE SHEET ARRANGEMENTS

We have no off-balance sheet arrangements.

RELATED PARTY TRANSACTIONS

There were no transactions with related parties during the quarter ended December 31, 2009.

CRITICAL ACCOUNTING POLICIES AND SIGNIFICANT ESTIMATES

Our unaudited interim consolidated financial statements are prepared in accordance with Canadian GAAP. These accounting principles require us to make certain estimates and assumptions. We believe that the estimates and assumptions upon which we rely are reasonable based upon information available at the time that these estimates and assumptions are made. Actual results could differ from these estimates. Significant areas requiring the use of estimates relate to the assessment for impairment and useful lives of intangible assets, determination of share value in transactions where shares are issued as a consideration, accrued liabilities, estimation of income tax expense and determination of fair value of stock-based compensation. The significant accounting policies that we believe are the most critical in fully understanding and evaluating the reported financial results include going concern assumption, intangible assets, stock-based compensation and income taxes. These and other significant accounting policies are described in *notes 1 and 2* of our annual consolidated financial statements and management discussion and analysis for the fiscal year ended March 31, 2009.

Changes in Significant Accounting Policies

Commencing April 1, 2009, we adopted recommendations of the CICA new Section 3064, “*Goodwill and Intangible Assets*”. This new section replaces Section 3062, “*Goodwill and Other Intangible Assets*” and Section 3450, “*Research and Development Costs*”. Various changes have been made to other sections of the CICA Handbook for consistency purposes. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. The adoption of these new standards did not have a material impact on our consolidated financial statements.

Commencing April 1, 2009, we also adopted guidance of the CICA EIC 173, “*Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*”. This guidance requires that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities including derivative instruments. This guidance is applicable to our financial periods ending on or after

January 20, 2009 with retrospective application without restatement of prior periods. The adoption of these new standards did not have a material impact on our consolidated financial statements.

New Accounting Pronouncements Affecting Future Periods

In February 2008, the Canadian Accounting Standard Board (the “AcSB”) confirmed that Canadian GAAP for public companies will be converged with International Financial Reporting Standards (“IFRS”) for accounting periods commencing on or after January 1, 2011. IFRS uses a conceptual framework similar to Canadian GAAP, but there are some significant differences on recognition, measurement and disclosures. We will be required to report under IFRS for interim and annual financial statements beginning April 1, 2011 and provide IFRS comparative figures for the preceding fiscal year, including an opening balance sheet as at April 1, 2010. We are currently planning for the conversion to IFRS and conducting a high-level preliminary assessment of the differences between Canadian GAAP and IFRS and the potential impact of IFRS to our financial reporting systems and processes.

In January 2009, the CICA issued Section 1601, “*Consolidations*” and Section 1602, “*Non-controlling Interests*”. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are applicable to interim and annual financial statements of the Company beginning on January 1, 2011. We are in the process of evaluating the impact of these standards.

In January 2009, the CICA issued Section 1582, “*Business Combinations*” replacing Section 1581, “*Business Combinations*”. The new section improves the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and its effects. The section is applicable to the annual and interim financial statements of the Company beginning on or January 1, 2011, with early adoption permitted. We are in the process of evaluating the impact of this standard.

RISKS AND UNCERTAINTIES

Due to the inherent nature of our business, investing in our securities involves a high degree of risk and uncertainties. Such risk factors include, among others, our stage of development, lack of product revenues, additional capital requirements, risk associated with completion of clinical trials and obtaining regulatory approval, dependence on collaborative partners, our ability to protect our intellectual property and our ability to stay competitive in a rapid changing industry environment.

We are in the early stage of development and have limited operating history. We have not generated any revenues to date from product sales, nor do we expect any product revenues for the immediate future. To achieve profitable operations, we must successfully develop our products that are currently in the research and development phase on our own or with collaborative partners. These product developments may take a number of years and involve significant risks and uncertainties. As a result, we require substantial additional capital to finance our product developments.

We are currently seeking additional capital to finance our operations. Management is considering all financing alternatives, including equity financing, debt arrangement and corporate collaboration, and has initiated discussions with our creditors to reduce or restructure our liabilities in order to enhance our financing ability. There can be no assurance that such financing will be materialized or be completed on a timely basis to allow us to continue as a going concern. If we are unable to obtain new funding, we may be required to cease our operations in the near term.

We are exposed to credit risks, interest rate risk, currency risk and liquidity risks as described in note 5 in our unaudited interim consolidated financial statements. We are also subject to other significant risks and uncertainties listed in the section titled “Risks and Uncertainties” in our annual MD&A for the year ended March 31, 2009 dated July 9, 2009 as well as the section titled “Risk Factors” in our Annual Information Form dated July 31, 2008.